

Decision **PROPOSED DECISION OF ALJ MILES** (Mail 12/23/2013)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SAN GABRIEL VALLEY WATER COMPANY (U337W) for Authorization to Issue and Sell Bonds, Notes, or Other Evidence of Indebtedness Not to Exceed \$80,000,000.

Application 13-05-006
(Filed May 13, 2013)

(See Appendix A for Appearances.)

**DECISION AUTHORIZING SAN GABRIEL VALLEY WATER COMPANY
TO ISSUE UP TO \$80 MILLION OF NEW LONG-TERM DEBT**

1. Summary

This decision grants San Gabriel Valley Water Company (SGVW) authority to issue up to \$80 million of long-term Debt Securities, as requested in Application 13-05-006. In its application, SGVW also requests an exemption from the New Financing Rule.¹ The exemption is denied.

2. Background

San Gabriel Valley Water Company (SGVW) is a public utility under the jurisdiction of this Commission, engaged in the business of producing, treating, storing, distributing and selling water service to approximately 93,000 customers

¹ Decision (D.) 12-06-015 dated June 7, 2012, authorized a new Financing Rule to replace the Competitive Bidding Rule. The Decision also revised and superseded General Order (GO) 24-B, and adopted GO 24-C, which changed the reporting requirements placed upon utilities, and eliminated the requirement that utilities maintain a separate bank account to record securities proceeds.

in portions of Los Angeles and San Bernardino Counties. SGVW's principal place of business is located at 11142 Garvey Avenue, El Monte, CA 91734.

SGVW filed Application (A.) 13-05-006 on May 13, 2013 seeking Commission authorization to issue up to \$80 million of Debt Securities in two or more financings. SGVW indicated that the net proceeds from the issuance would be used to reimburse its treasury for monies expended for the design, construction, completion, extension or improvement of utility plan facilities and to repay short-term indebtedness incurred for such purposes.

2.1. Procedural Matters

By Resolution ALJ 176-3315, dated May 23, 2013, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings would not be necessary. The Office of Ratepayer Advocates (ORA)² filed a protest to the application on June 13, 2013. SGVW filed a reply to the protest on June 24, 2013. ORA withdrew its protest on August 12, 2013.

A prehearing conference (PHC) was held in San Francisco on September 18, 2013. SGVW appeared and was represented by counsel. Two attorneys appeared on behalf of ORA. During the PHC, David M. Batt, the Vice President and Treasurer of SGVW, gave testimony concerning the application, and provided details concerning the manner in which SGVW obtains financing and uses debt enhancement features to obtain the best possible terms from prospective lenders. Therefore, although the matter was initially designated as

² The Division of Ratepayer Advocates was renamed the Office of Ratepayers Advocates (ORA) effective September 26, 2013, pursuant to Senate Bill 96 (Budget Act of 2013), which was approved by the Governor on September 26, 2013. The statutory mission of the ORA is to obtain the lowest possible rate for service consistent with reliable and safe service levels. In fulfilling this goal, ORA also advocates for customer and environmental protections.

“no hearing required”, a hearing was held at which a witness testified and was cross examined.³ SGVW filed a brief in support of its application on September 25, 2013. ORA filed a brief in support of the application on October 2, 2013.

3. Request

SGVW seeks authorization to issue up to \$80 million of Debt Securities through the issuance and sale of Debt Securities in two or more financings. The precise amount and timing of each financing, the market to be used and method by which it will be effected, price and interest rate (which may be fixed, adjustable, or variable), and other material provisions of the Debt Securities issued in each financing will be determined by SGVW with due regard for its financial condition, requirements and the then prevailing and anticipated market conditions, including competing demands for funds, existing at the time of each financing. Debt Securities would consist of First Mortgage Bonds, debentures and promissory notes, medium-term notes and loans.

3.1. First Mortgage Bonds

First Mortgage Bonds would be issued in conformity with provisions of, and secured by, SGVW’s Trust Indenture, dated September 1, 1945, as amended and supplemented. First Mortgage Bonds may be placed privately and may have fixed or floating rates of interest, and may have sinking fund provisions.

3.2. Debentures and Promissory Notes

Debentures or promissory notes may be placed privately and may have fixed or floating rates of interest. Such debentures or promissory notes would be issued in accordance with an indenture, purchase agreement, or other document

³ The parties agreed to provide briefing following the PHC and have already done so, therefore, no scoping memo was required under the Commission’s Rules of Practice and Procedure, Rule 7.3(b).

that would set forth the aggregate principal amount, maturity, default, and other material provisions of such debentures or promissory notes.

3.3. Medium-Term Notes

Medium-term notes may be offered on a continuous or periodic basis. Maturities generally would range from twelve months to 10 years⁴, although they may extend for more than 30 years. They may be sold in private offerings, with fixed or floating rates, in senior or subordinated form. Medium-term notes can be tailored to an investor's specific maturity needs so as to achieve the lowest available cost of funds.

3.4. Loans

SGVW may, from time to time, borrow directly from banks, insurance companies, or other sources. SGVW intends to confine its borrowing of this nature to situations designed to result in lower overall cost of funds and/or more advantageous terms and conditions than currently would be available through the issuance of other types of Debt Securities.

3.5. Debt Enhancement Features

SGVW seeks authorization to enter into debt enhancement features which will permit it to take advantage of market opportunities and adjustments to pricing in order to obtain low-cost debt financing. SGVW indicates that it will use debt enhancement features only if, in its discretion and judgment, the feature is likely to, under then current market conditions, reduce the overall cost of money for the benefit of ratepayers. Potential debt enhancement features that SGVW may use are delayed drawdowns, redemption provisions, sinking funds,

⁴ Page 5 of SGVW's application describes the maturity period for medium-term notes as "nine months to 10 years." However, during testimony, SGVW's Vice President and Treasurer, Mr. Batt, confirmed that medium term notes would be one year or more. (Testimony, page 19, lines 14-28 through page 20, line 5.)

tax exemption options, treasury locks, all of which are permissible under the New Financing Rule.

4. Discussion

SGVW's request to issue Debt Securities is subject to §§ 816 *et seq.* of the Public Utilities Code.⁵ The Commission has broad discretion under §§ 816 *et seq.* to determine if a utility should be authorized to issue debt. Where necessary and appropriate, the Commission may attach conditions to the issuance of debt to protect and promote the public interest.

Prior to June 7, 2012, the Commission required public utilities to sell debt securities through a competitive bidding process.⁶ However, as the frequency of requests for exemption from competitive bidding increased, the Commission deemed it appropriate to authorize a new Financing Rule. In D.12-06-015, dated June 7, 2012, the Commission authorized utilities to choose whether to issue debt via competitive or negotiated bid, as long as the method chosen achieves a lower cost of capital. The Decision also revised and superseded GO 24-B and adopted GO 24-C, which changed the reporting requirements placed upon utilities, and

⁵ All statutory references are to the Public Utilities Code unless otherwise stated. Pub. Util. Code § 816 states: "The power of public utilities to issue stocks and stock certificates or other evidence of interest or ownership and bonds, notes, and other evidences of indebtedness and to create liens on their property situated within this State is a special privilege, the right of supervision, regulation, restriction, and control of which is vested in the State, and such power shall be exercised as provided by law under such rules as the commission prescribes."¹

⁶ D.38614 issued January 15, 1946, established the Competitive Bidding Rule for utilities issuing new securities. The Competitive Bidding Rule was last amended on October 1, 1986, in Resolution F-616. Since that time, the Commission has permitted utilities to seek an exemption from the Competitive Bidding Rule for debt issues in excess of \$200 million, upon a compelling showing that, because of the size of the issues, an exemption was warranted to deviate from competitive bidding to take advantage of market opportunities, i.e., via negotiated bidding.

eliminated the requirement that utilities maintain a separate bank account to record securities proceeds.

4.1. Debt Securities

In its application, SGVW states that it intends to apply the net proceeds from the proposed \$80 million issuance of Debt Securities to reimburse its treasury for monies expended and to be expended, for the design, construction, completion, extension, or improvement of utility plant facilities and to repay short-term indebtedness incurred for such purposes. SGVW attaches the following Exhibits to its application in support of its request: 1) Exhibit A - Financial Statement through December 31, 2012; 2) Exhibit B - Total Capitalization and Capital Ratios; 3) Exhibit C - Supplemental Financial Information. Exhibit C includes SGVW's Construction Budgets for the years 2013 - 2015.

SGVW has substantiated that the requested authorization is necessary to satisfy its needs for financing capital expenditures, a proper purpose under § 817⁷ for issuing debt. Moreover, as required by § 818,⁸ these expenditures are not reasonably chargeable to operating expenses or income. Therefore, we will grant

⁷ Pub. Util. Code § 817 - A public utility may issue stocks and stock certificates or other evidence of interest or ownership, and bonds, notes, and other evidences of indebtedness payable at periods of more than 12 months after the date thereof, for any one or more of the following purposes and no others:⁺

(a) For the acquisition of property.⁺

(b) For the construction, completion, extension, or improvement of its facilities.⁺

(c) For the improvement or maintenance of its service.⁺

(d) For the discharge or lawful refunding of its obligations.⁺

(e) For the financing of the acquisition and installation of electrical and plumbing appliances and agricultural equipment which are sold by other than a public utility, for use within the service area of the public utility.⁺

(f) For the reorganization or readjustment of its indebtedness or capitalization upon a merger, consolidation, or other reorganization.⁺

(g) For the retirement of or in exchange for one or more outstanding stocks or stock certificates or other evidence of interest or ownership of such public utility, or bonds, notes, or other evidence of indebtedness of such public utility, with or without the payment of cash.⁺

(h) For the reimbursement of moneys actually expended from income or from any other money in the treasury of the public utility not secured by or obtained from the issue of stocks or stock certificates or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness of the public utility, for any of the aforesaid purposes except maintenance of service and replacements, in cases where the applicant has kept its accounts and vouchers for such expenditures in such manner as to enable the commission to ascertain the amount of money so expended and the purposes for which such expenditure was made.

⁸ Pub. Util. Code § 818 - No public utility may issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months after the date thereof unless, in addition to the other requirements of law it shall first have secured from the commission an order authorizing the issue, stating the amount thereof and the purposes to which the issue or the proceeds thereof are to be applied, and that, in the opinion of the commission, the money, property, or labor to be procured or paid for by the issue is reasonably required for the purposes specified in the order, and that, except as otherwise permitted in the order in the case of bonds, notes, or other evidences of indebtedness, such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

SGVW authority to issue up to \$80 million of long-term debt for its required purposes, as detailed in the application.

Consistent with § 824,⁹ SGVW shall maintain records to identify the specific long-term debt issued pursuant to this decision, and demonstrate that proceeds from such debt have been used only for the purposes authorized by this decision.

4.2. Request for Exemption from New Financing Rule

The Commission last reviewed and approved an SGVW application for authorization to issue and sell bonds, notes and other evidence of indebtedness in 2008.¹⁰ At that time, SGVW sought and was granted an exemption from the Competitive Bidding Rule,¹¹ noting that: (1) SGVW did not have a bond rating; (2) the Commission had granted SGVW and other utilities similar exemptions and modifications with no discernable adverse impacts on the utilities, their customers, or the public at large; and (3) SGVW represented that granting the exemption would enable it to obtain debt in a manner advantageous to SGVW and its ratepayers.

⁹ Pub. Util. Code § 824 - The commission may require public utilities to account for the disposition of the proceeds of all sales of stocks and stock certificates or other evidence of interest or ownership, and bonds, notes, and other evidences of indebtedness, in such form and detail as it deems advisable, and may establish such rules as it deems reasonable and necessary to insure the disposition of such proceeds for the purposes specified in its order.

¹⁰ See D.08-07-018, issued July 11, 2008.

¹¹ The Competitive Bidding Rule was enacted in 1946 and was last amended via Resolution F-616 issued on October 1, 1986. It required utilities with bond ratings of "A" or higher to issue debt using competitive bids. The purpose of the Rule was to reduce the cost of debt issued by utilities. The Resolution permitted utilities to seek an exemption from the Competitive Bidding Rule for debt issues in excess of \$200 million, upon a compelling showing that, because of the size of the issues, an exemption was warranted.

At that time, SGVW reasoned that, because it is a privately held company and relatively small size utility that infrequently participates in the capital and debt markets, a negotiated offering would permit it to obtain lower costs than competitive bidding. SGVW explained that, when it finds it necessary to issue debt securities, it does so through a process of private placement with institutional lenders such as large insurance companies which historically, have purchased water utility company bond issues.

Since the last amendment of the Competitive Bidding Rule in 1986, the Commission has, on many occasions, granted exemptions to individual utilities in order to permit them to take advantage of market opportunities and has authorized utilities to enter into debt enhancement arrangements in order to improve the terms and conditions of new issuances of debt securities and to lower the overall cost of money for the benefit of ratepayers. As a result, the Commission entirely replaced the Competitive Bidding Rule with a new Financing Rule and General Order 24-C, set forth in D.12-06-015, effective June 7, 2012 (New Financing Rule).

One rationale for the New Financing Rule, expressed by the Commission in 2012, was “to grant utilities the discretion to choose whether to issue debt via competitive or negotiated bid, so long as the basis for the method chosen would achieve the lowest cost of capital.” This rationale is consistent with, not adverse to, SGVW’s interests in seeking negotiated offerings.

The New Financing Rule also: 1) required utilities with \$25 million or more of operating revenues to make every effort to encourage, assist and recruit Women owned, Minority owned, and disabled Veteran owned Business Enterprises (WMDVBE) in being appointed as lead underwriter, book runner or co-manager of debt offerings; 2) eliminated the notification and form of

communication requirement for the solicitation of bids; 3) eliminated the requirement that a utility maintain a separate bank account to record securities proceeds; 4) set requirements for the use of Debt Enhancement Features; 5) provided additional exemptions applicable to use of the New Financing Rule, and 6) implemented General Order 24-C to revise the interval of required reporting (changed from monthly to quarterly, then semi-annual reporting) as well as the type of information that must be provided in the reporting.

The above six provisions of the New Financing Rule, are consistent with SGVW's reported needs and practices. For instance, although SGVW explains that its bond issues have not required managers, underwriters or book runners, and that its typical private placement process with institutional lenders (such as large insurance companies) historically are not likely to be WMDVBE, SGVW's application represents that SGVW will use its best efforts to encourage the participation of diverse suppliers in any transaction conducted under the authorization requested in this application. We note that SGVW indicates that it has a supplier diversity program under which it awarded 11.5% of its 2012 annual procurement expenditures to WMDVBE firms. Therefore, we find that SGVW satisfies the requirement of the New Financing Rule, that utilities "make every effort to encourage, assist and recruit WMDVBE."

GO 24-B required utilities to submit monthly reporting to the Commission about the amount of debt issued and outstanding during the previous month; (ii) the purposes for which the utility expended the proceeds realized from the issuance of debt during the prior month; and (iii) a monthly statement of the separate bank account that the utility was required to maintain for all receipts and disbursements of money obtained from the issuance of debt.

The Commission previously granted SGVW and other utilities an exemption from the reporting requirements to permit reporting required by GO 24-B on a quarterly rather than monthly basis.¹² The New Financing Rule and GO 24-C implemented by D.12-06-015 now requires only quarterly reporting by all utilities. Additionally, utilities are no longer required to maintain a separate bank account to record securities proceeds.

SGVW does not require an exemption from this aspect of the New Financing Rule since SGVW's practices and needs, that previously led SGVW to request exemption from the Competitive Bidding Rule and GO-24-B, are consistent with the rule.

The New Financing Rule now authorizes utilities to use debt enhancement features to improve the terms and conditions of their long-term debt securities and to lower the overall cost of money, which in turn, benefits the ratepayers. In its reply to the Protest¹³ of ORA, in its testimony by its Vice President-Treasurer, and in its brief following the PHC, SGVW states that it is in compliance with the New Financing Rule requirement that a utility proposing the potential use of debt enhancement features in a financing application, "provide a brief description and rationale for the potential use of a debt enhancement." SGVW further indicates that it will make every effort to comply with the New Financing Rule when completing any issuance of debt.¹⁴ SGVW's application provides a brief description and rationale for four debt enhancement features – Delayed Drawdown, Redemption Provisions, Sinking Funds and Tax Exemptions – that it may wish to use. SGVW has not requested relief from any specific aspect of the

¹² See D.08-07-018.

¹³ ORA filed a Protest to the application on June 13, 2013, but withdrew its protest on August 12, 2013 and filed a Reply brief supporting the application on October 2, 2013.

¹⁴ See Reply to Protest dated June 24, 2013; Testimony of David Batts, PHC Transcript at 16, lines 20-27; Brief of SGVW dated September 25, 2013.

New Financing Rule requirements which pertain to debt enhancement features and preliminarily, has complied with the requirements.

SGVW indicates that it does not anticipate the need to borrow/obtain debt capital exceeding \$40 million at any one time, and on that basis, requests exemption from the New Financing Rule. However, the New Financing Rule was implemented to provide the flexibility that SGVW is employing. Therefore, SGVW's request for exemption from the New Financing Rule should not be granted because the request is not supported by a compelling showing, regardless of whether SGVW anticipates that one or more of its proposed debt issuances will be less than \$40 million.

4.3. California Environmental Quality Act (CEQA) Review

SGVW expects that it will use the entire \$80 million proposed financing proceeds for construction expenditures, repaying short-term indebtedness for such purposes, and reimbursing SGVW for money it has expended for those purposes. This decision does not authorize any capital expenditures or construction projects. New construction projects which SGVW intends to finance via this application should undergo a CEQA review as early as feasible in the planning process, as required by CEQA Guidelines Section 15004(b). To the extent capital expenditures are financed with the proceeds of the long-term debt issued pursuant to this decision, CEQA review should occur as needed through the regulatory processes applicable to each capital project.

5. Fee

Public Utilities Code Sections 1904(b) and 1904.1 require the Commission to charge and collect a fee whenever it authorizes a utility to issue debt and preferred stock. A fee is not applicable on any such issues used to guarantee,

take over, refund, discharge, or retire any stock, bond, note, or other evidence of indebtedness on which a fee has already been paid to the Commission.

SGVW expects to use the full amount of the proposed financing proceeds for construction expenditures and acquisition of property, or to reimburse itself for money it has expended for those purposes. Therefore, the full \$80 million of long-term debt authorized hereunder is subject to a fee.

The fee applicable to SGVW shall be calculated as follows:

First \$1,000,000 charged @ \$2.00 per \$1,000	\$ 2,000
\$1,000,000 up to ten million charged @ \$1.00 per \$1,000	\$ 9,000
Over ten million charged @ \$0.50 per \$1,000	<u>\$35,000</u>
Total fee applicable to SGVW	\$46,000

SGVW shall remit the required \$46,000 fee to the Commission's Fiscal

Office and the authority granted by this decision shall not become effective until SGVW remits the fee.

6. Category and Need for Hearing

By Resolution ALJ 176-3315, dated May 23, 2013, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings would not be necessary.

During the PHC held September 18, 2013, an SGVW witness testified and was cross-examined, thereby transforming the PHC into an evidentiary hearing. Therefore, although the matter was initially designated as "no hearing required," a hearing was required and occurred. Based on the record, we affirm that this is a ratesetting proceeding, however, we change the preliminary determination that "no hearing is required" to "hearing is required."

7. Reduced Comment Period

This is an uncontested matter which does not require a comment period pursuant to Public Utilities Code Section 311(g)(3). However, pursuant to Rule

14.6(b) of the Commission's Rules of Practice and Procedure, SGVW has requested and was granted a ten (10) day period for public review and comment.

~~Accordingly, No~~ comments were filed ~~on December _____, 2013 and reply comments were filed on January _____, 2014.~~

8. Assignment of Proceeding

Catherine J.K. Sandoval is the assigned Commissioner and Patricia B. Miles is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. SGVW seeks authority to issue up to \$80 million of new Debt Securities in two or more financings.
2. ORA protested this application, but that protest has been withdrawn.
3. SGVW has a reasonable need to issue \$80 million of long-term debt to finance capital expenditures.
4. SGVW seeks authority to issue different types of Debt Securities utilizing negotiated bidding and debt enhancement features when appropriate to obtain terms that should reduce the overall cost of money for the benefit of its ratepayers.
5. D.12-06-015 authorizes SGVW to choose whether to issue debt via competitive or negotiated bid and to utilize debt enhancement features.
6. GO 24-C authorizes SGVW to report on a quarterly basis the information required by GO 24-B in order to reduce its administrative and compliance costs.
7. GO 24-C eliminates the requirement that SGVW maintain a separate bank account to record securities proceeds.
8. A.13-05-006 does not propose, and today's decision does not authorize, any specific new construction or changes in use of existing assets and facilities.

9. Resolution ALJ 176-3315, preliminarily determined that this proceeding should be categorized as ratesetting with no need for hearings.

10. An Evidentiary Hearing was held on September 18, 2013, therefore this proceeding should be categorized as requiring a hearing.

Conclusions of Law

1. This is a ratesetting proceeding.
2. There is a need for hearing.
3. The request for authorization to issue up to \$80 million of long-term debt securities should be granted.
4. The request for exemption from D.12-06-015 should be denied.
5. The authority granted by this decision should not become effective until SGVW has paid the fees prescribed by §§ 1904(b) and 1904.1.
6. SGVW should report the information required by GO 24-C, on a quarterly basis.
7. SGVW should not use the proceeds from the debt authorized by this decision to fund capital projects until SGVW has obtained any required Commission approvals for the projects, including any required environmental review under CEQA.
8. The following Order should be effective immediately so that SGVW may issue the debt authorized herein as soon as needed.

O R D E R

IT IS ORDERED that:

1. San Gabriel Valley Water Company is authorized to issue \$80 million of new long-term debt to finance capital expenditures and to repay short-term

indebtedness and to reimburse its treasury for monies expended for such purposes.

2. San Gabriel Valley Water Company is not exempted from the requirements of the Commission's New Financing Rule and General Order 24-C as adopted in Decision 12-06-015.

3. San Gabriel Valley Water Company must report on a quarterly basis all the information required by General Order 24-C with respect to debt issued pursuant to this Order.

4. San Gabriel Valley Water Company must remit fees of \$46,000 to the Commission as required by § 1904(b) of the Public Utilities Code. The decision number of this Order must appear on the face of the check.

5. The authority granted by this Order is not effective until San Gabriel Valley Water Company remits the fees to the Commission pursuant to Ordering Paragraph 4.

6. San Gabriel Valley Water Company must comply with all applicable environmental laws and regulations when planning and implementing any capital expenditure programs that are financed, in whole or in part, with the proceeds from the debt authorized by this Order.

7. The hearing determination is changed to "hearings are necessary."

8. Application 13-05-006 is closed.

This order is effective today.

Dated _____, 2014 at San Francisco, California.

APPENDIX A

***** **Appearances** *****

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(END OF APPENDIX A)

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